



This document is scheduled to be published in the Federal Register on 08/21/2014 and available online at <http://federalregister.gov/a/2014-19832>, and on FDsys.gov

DEPARTMENT OF LABOR

Employee Benefits Security Administration

29 CFR Parts 2520 and 2550

RIN 1210-AB59

Request for Information Regarding Standards for Brokerage Windows in Participant-Directed Individual Account Plans

AGENCY: Employee Benefits Security Administration, Department of Labor.

ACTION: Request for information.

SUMMARY: The Employee Benefits Security Administration of the U.S. Department of Labor (the Department) is publishing this Notice as part of its review of the use of brokerage windows (including self-directed brokerage accounts or similar arrangements) in participant-directed individual account retirement plans covered by the Employee Retirement Income Security Act of 1974 (ERISA). Some plans offer participants access to brokerage windows in addition to, or in place of, specific investment options selected by the plans' fiduciaries. Through these arrangements, plan participants may be able to choose among the full range of investment options available in the investment marketplace. The Request for Information contained in this

Notice will assist the Department in determining whether, and to what extent, regulatory standards or other guidance concerning the use of brokerage windows by plans are necessary to protect participants' retirement savings. It also will assist the Department in preparing any analyses that it may need to perform pursuant to Executive Order 12866, the Paperwork Reduction Act, and the Regulatory Flexibility Act.

DATES: Comments must be submitted on or before [ENTER DATE THAT IS 90 DAYS AFTER THE DATE OF PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: You may submit written comments to any of the addresses specified below.

- Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments.
- E-mail: e-ORI@dol.gov. Include RIN 1210-AB59 (Brokerage Windows RFI) in the subject line of the message.
- Mail: Office of Regulations and Interpretations, Employee Benefits Security Administration, Room N-5655, U.S. Department of Labor, 200 Constitution Avenue, NW, Washington, DC 20210, Attention: "Brokerage Windows RFI."

All submissions received must include the agency name and Regulation Identifier Number (RIN) for this rulemaking. Comments received will be posted without change to <http://www.regulations.gov> and <http://www.dol.gov/ebsa>, and made available for public inspection at the Public Disclosure Room, N-1513, Employee Benefits Security Administration,

200 Constitution Avenue, NW, Washington, DC 20210, including any personal information provided. Do not include any personally identifiable information (such as name, address, or other contact information) or confidential business information that you do not want publicly disclosed. Comments posted on the Internet can be retrieved by most Internet search engines. Comments may be submitted anonymously. Persons submitting comments electronically are encouraged not to submit paper copies. All comments will be made available to the public.

FOR FURTHER INFORMATION CONTACT: Kristen Zarenko, Office of Regulations and Interpretations, Employee Benefits Security Administration, (202) 693-8500. This is not a toll-free number.

SUPPLEMENTARY INFORMATION:

A. Background

Retirement plans that allow participants to choose investments for their individual accounts typically offer a limited set of specific investment options, which are selected and monitored by a plan fiduciary. Some plans also offer brokerage windows, which enable participants to select investment options beyond those specifically designated by the plan fiduciary. In some cases, the brokerage window may be offered in place of any designated investment options. The use of brokerage windows and similar arrangements by participant-directed individual account retirement plans (such as 401(k) plans) raises important issues

concerning ERISA's reporting and disclosure requirements, as well as ERISA's fiduciary standards.

The Department addressed disclosure requirements for brokerage windows in a regulation requiring plan administrators to disclose certain plan and investment-related information to participants and beneficiaries in participant-directed individual account plans (the “participant-level disclosure regulation”).¹ This regulation was intended to ensure that all participants and beneficiaries in such plans have the information they need to make informed decisions about the management of their individual accounts and the investment of their retirement savings. To that end, the regulation requires that, at least annually, participants and beneficiaries are furnished a comparative chart (or similar format) that contains information about the plan's “designated investment alternatives.” Plan administrators must, for example, furnish fee, historical performance, and comparative benchmark information for each designated investment alternative.

The regulation expressly provides that brokerage windows are not “designated investment alternatives.”² As a result, plan administrators are not required to disclose the detailed performance, fee, and other investment-related information required with respect to “designated investment alternatives.” Instead, plan administrators must provide “a description of any

¹ 75 FR 64910 (Oct. 20, 2010), codified at 29 CFR § 2550.404a-5, and including conforming changes to the Department's “404(c) regulation” relating to plans that allow participants to direct the investment of their individual accounts, at 29 CFR § 2550.404c-1.

² The regulation defines a “designated investment alternative” to mean: “[A]ny investment alternative designated by the plan into which participants and beneficiaries may direct the investment of assets held in, or contributed to, their individual accounts. The term “designated investment alternative” *shall not include* ‘brokerage windows,’ ‘self-directed brokerage accounts,’ or similar plan arrangements that enable participants and beneficiaries to select investments beyond those designated by the plan.” 29 CFR § 2550.404a-5(h)(4) (emphasis added).

‘brokerage windows,’ ‘self-directed brokerage accounts,’ or similar plan arrangements that enable participants and beneficiaries to select investments beyond those designated by the plan.’³ In addition, the plan administrator must provide an explanation of any fees and expenses that may be charged against an individual account, on an individual, rather than on a plan-wide, basis, in connection with the arrangement. Finally, participants must be furnished a statement of the dollar amount of the fees and expenses charged to their accounts in connection with the arrangement during the previous quarter.⁴

Following publication of the participant-level disclosure regulation, plan sponsors and administrators raised a number of questions about the regulation, including how it applied to brokerage windows. These questions concerned both the required disclosures for brokerage windows as well as other fiduciary obligations that may arise when a plan offers a brokerage window. In response, the Department provided a series of “frequently asked questions” about the participant-level disclosure regulation. These questions and answers were published in Field Assistance Bulletin 2012-02R (FAB).⁵ FAB Question 13 describes the information about brokerage windows that must be furnished to participants and beneficiaries in order to satisfy section (c)(1)(i)(F) of the regulation, which requires a “description” of the brokerage window. The FAB lists specific information requirements, including instructions for participants on how to use the plan’s brokerage window, any restrictions on trading within the brokerage window, and fees and expenses that may be charged in connection with using the brokerage window (*e.g.*,

³ 29 CFR § 2550.404a-5(c)(1)(i)(F).

⁴ 29 CFR § 2550.404a-5(c)(3)(ii)(A).

⁵ <http://www.dol.gov/ebsa/regs/fab2012-2R.html>.

annual fees for using the brokerage window feature, brokerage or other commissions for trades within the brokerage window).

FAB Question 39⁶ clarifies that a brokerage window is not *itself* a “designated investment alternative” under a plan. The Department also explains in Question 39 that a plan fiduciary’s failure to designate investment alternatives, for example, by offering no menu of core investment options other than a brokerage window to avoid the regulation’s investment-related disclosure requirements, may raise questions under ERISA’s section 404 general statutory duties of prudence and loyalty. The Department issued this cautionary statement based, in part, on its observation that brokerage window features were being marketed by some to plan fiduciaries as a device to avoid making participant investment disclosures required under the regulation.

The Department is aware that plan fiduciaries and service providers continue to have questions about their duties under ERISA’s general fiduciary standards apart from the specific requirements of the participant-level disclosure regulation. The Department is committed to engage in discussions with interested parties to help determine how best to assure compliance with these duties in a practical and cost-effective manner. This includes considering whether amendment of relevant regulatory provisions or interpretive guidance may be appropriate and necessary to ensure that participants and beneficiaries with access to brokerage windows are adequately protected.

⁶ The original version of the FAB, which was rescinded and replaced by FAB 2012-02R, included Question 30, which some viewed as raising the possibility that plan fiduciaries could be responsible under ERISA for the underlying investments into which participants invest through a brokerage window. Further, some plan sponsors and service providers stated that the Department should not have issued Question 30 without prior notice and opportunity for public comment. Although the Department disagreed, it withdrew the original FAB. The revised FAB replaced Question 30 with Question 39, which is described in this Notice.

Since issuance of the FAB, the Department has reviewed literature, articles and other commentary available on the use of brokerage windows in 401(k) plans. The Request for Information contained in this Notice (the RFI) is the Department's next step in increasing its understanding of this topic.

Some articles make the case that brokerage windows can be highly attractive and suitable plan features for sophisticated investors. These individuals assert that participants with a more advanced understanding of the investment marketplace, including the various costs and risks associated with investing in different types and classes of securities, may benefit from brokerage windows and the ability to create a better customized, more diverse portfolio. Brokerage windows may, for example, provide access to a specialized asset class or classes not available through the plan's core designated investment alternatives. Sophisticated investors may be less likely to be overwhelmed by a large number of investment options and may benefit from the flexibility that brokerage windows offer.

Some articles make the case that brokerage windows actually benefit rank-and-file participants by indirectly limiting the field. These individuals assert that many plans over time have increased the number of designated investment alternatives they offer in response to demands from company owner-employees, senior executives, and other potentially sophisticated employee-investors for access to more diverse investment opportunities. This results in some plans having a very large number of designated investment alternatives, which may confuse less knowledgeable participants. Making a brokerage window available to the more demanding

employees enables plans to offer a more manageable number of designated investment alternatives to rank and file employees who, according to those proponents of brokerage windows, have little or no interest in investment opportunities beyond a basic set of diversified options.

Other articles, however, counter that brokerage windows may present undue risks for many retirement plan participants, because plan fiduciaries do not engage in a deliberative process to affirmatively review and select each of the investment options available through brokerage windows. Thus, they say in the absence of a deliberative review and selection process by an ERISA fiduciary, participants may not have adequate or any protections against potentially costly or unsuitable investments made through the brokerage window. Opponents maintain, for example, that the same or similar investments often cost more when selected through a brokerage window as opposed to when they are designated by the plan. Brokerage window opponents maintain that plans have no bona fide method to restrict brokerage window access only to sophisticated participants, and that the use of dollar thresholds or gateways, for example, may discriminate in favor of highly compensated employees. Opponents further maintain that although it is permissible to do so, brokerage window operators rarely limit the investments they make available. Opponents also allege that in-plan investments often subsidize the administrative costs of participants who opt to use the brokerage window.

B. Request for Information

The purpose of this RFI generally is to increase the Department's understanding of the prevalence and role of brokerage windows in participant-directed individual account plans covered by ERISA. In particular, the RFI will focus on why, under what circumstances, and how often these brokerage windows are offered and used in ERISA plans, and the legal and policy issues that relate to such usage. The Department wants to make sure that participants are not exposed to undue risks from brokerage windows and that plan fiduciaries properly understand the scope of their ongoing responsibilities with respect to brokerage windows. The information received in response to this RFI will assist the Department in determining whether, and to what extent, regulatory standards or safeguards, or other guidance, are necessary to protect participants' retirement savings. The RFI contains a number of questions. Respondents need not answer every question, but should identify, by its number, each question addressed. Interested persons also are encouraged to address any other matters they believe to be germane to the general topic of this RFI.

Defining “Brokerage Windows” – Scope. The Department understands that a variety of different plan and investment arrangements may be encompassed by the terms “brokerage window,” “self-directed brokerage account,” and similar arrangements. For example, open mutual fund windows may permit participants to invest in hundreds or thousands of mutual funds. More limited mutual fund windows or “supermarkets” may permit participants to invest in any mutual fund on one or more of a particular vendor's platforms, but not necessarily every mutual fund on the market. Other brokerage accounts also offer participants access to a virtually unlimited number of individual stocks, exchange-traded funds, and other securities.

1. What are the various brokerage window, self-directed brokerage account, and similar arrangements that are made available in 401(k) plans, and which one (or more) is the most common? What are the benefits and drawbacks of these various arrangements?
2. If a more specific definition of a “brokerage window” is provided, as a regulatory or interpretive matter, how should it be defined?
3. Should the fiduciary, disclosure, or other standards that apply to brokerage windows (and which are raised in more detail below) vary depending on the type of arrangement, or perhaps the ultimate number of investment options available to participants (*e.g.*, a mutual fund window that offers access to fifty mutual funds vs. an open brokerage structure that offers access to many thousands of stocks, mutual funds, and other securities) and, if so, how?

Plan Investment Offerings – Brokerage Windows and Designated Investment Alternatives.

4. What are the characteristics of plans that offer brokerage windows?
5. Is the number of plans offering brokerage windows increasing, decreasing, or remaining relatively constant? If the number is changing, why?
6. What is a typical number of “designated investment alternatives” offered by a 401(k) plan? Are plans increasing, decreasing, or holding constant the number of designated investment alternatives that they offer? If the number is changing, why?
7. Is there any correlation between the trends observed in the preceding two questions, and if so, what is the correlation?

8. At what point might the number of investment options available to plan participants warrant treating the options as a “brokerage window” of some variety, rather than as a menu of “designated investment alternatives?” Does the detailed investment-related information required by the Department’s participant-level disclosure regulation for designated investment alternatives (vs. brokerage windows) affect the answer to this question and, if so, how?

Participation in Brokerage Windows.

9. How many participants, or what proportion of participants, typically use their plan’s brokerage window? What proportion of a plan’s total assets typically is invested through the brokerage window?
10. Do respondents have demographic data on these participants, either for a particular plan or more broadly?
11. Of the participants that use their plan’s brokerage window, do these participants typically invest all of the assets in their plan account through the window, or some proportion of their assets?
12. What types of restrictions, if any, are typically made on brokerage window participation (e.g., minimum account balances, minimum dollar amounts that may be transferred to a brokerage window, maximum percentage of account balance that may be invested through a brokerage window, etc.)?
13. Is there evidence of good or poor decision-making and outcomes by those participants using brokerage windows? What types of evidence are available?

14. What benefits accrue to participants that invest through brokerage windows? Do participants who do not invest through the brokerage window benefit from having a brokerage window option in their plan, and if so, how?

Selecting and Monitoring Brokerage Windows and Service Providers.

15. How many vendors does a plan fiduciary research or contact, on average, when deciding whether to include a brokerage window feature? How do vendors typically market brokerage windows to their existing or potential plan clients?
16. Do plan recordkeepers typically require the use of their own or affiliated brokerage services, or are plan fiduciaries able to shop for brokerage windows provided by multiple vendors? Are there ways in which brokerage window providers favor or encourage investment in proprietary funds or products through brokerage windows?
17. What factors do plan fiduciaries consider and what challenges, if any, do they face when deciding whether to include a brokerage window and who should provide the window?
18. What are the most common reasons for adding a brokerage window feature (*e.g.*, flexibility and increased investment options for participants, to facilitate the ability of participants to work with an adviser or a managed account provider, etc.)? What role, if any, do concerns about fiduciary responsibility or disclosure obligations play in deciding whether to add a brokerage window?
19. When a plan fiduciary selects a brokerage window feature for a plan, does the plan fiduciary typically enter into a contract for this service, on behalf of the plan? If so, who are the parties to the contract? If not, why not?

20. Do plan participants themselves commonly contract with the vendor when they choose to participate in the brokerage window (either in lieu of, or in addition to, a contract with a plan official) and, if so, what role, if any, does a plan fiduciary play in this process?
21. What role, if any, do plan fiduciaries play in the selection of brokers, advisers, or other service providers to a brokerage window? How do plan fiduciaries monitor the performance of these service providers if at all?

Fiduciary Access to Information about Brokerage Window Investments.

22. How do plan fiduciaries monitor investments made through their plan's brokerage window, if at all? For example, do plan fiduciaries have access to information about specific investments that are selected or asset class or allocation information?
23. Do fiduciaries view this information as important to effectively monitoring the inclusion of a brokerage window feature in their plan? If applicable, how often do plan fiduciaries request and review such information?
24. What, if any, technological or other challenges exist that may reduce the feasibility, or increase the cost, of compiling this type of information for plan fiduciaries? Can respondents quantify such costs?

Brokerage Window Costs.

25. What are the most common costs associated with participation in a brokerage window (e.g., account fees, brokerage commissions, etc.), and what dollar amounts are typically

charged? Are there costs to including a brokerage window that usually are borne by the plan sponsor or by the plan, rather than by individual participants who use the brokerage window?

26. To what extent are brokerage windows effectively subsidized by plan participants other than those participating in the brokerage window?
27. How do the costs of investing through a brokerage window typically compare to investing in a plan's designated investment alternatives? How do the costs compare to investing outside of the plan, *e.g.*, in an IRA?
28. How significant of a factor to plan fiduciaries are these costs when deciding to add a brokerage window to their plan? How do plan fiduciaries monitor or oversee the fees and costs of a brokerage window, available investments, and related services? How much discretion does a plan fiduciary have in negotiating brokerage commissions and other costs that presumably cannot be controlled by participants?

Disclosure Concerning Brokerage Windows and Underlying Investments.

29. Is the information required to be disclosed about brokerage windows by the Department's participant-level disclosure regulation sufficient to protect plan participants? Is this required information more or less than plans disclosed prior to the effective date of the regulation? Does this information usually come from plan administrators or from a third party, such as plan service or investment providers? What additional information, if any, is or should be disclosed to participants?

30. Is different or additional information disclosed to participants after they elect to participate in a brokerage window and, if so, what information?
31. The Department has said that disclosures regarding brokerage windows or similar arrangements under the participant-level fee disclosure regulation must, at a minimum, provide sufficient information to enable participants and beneficiaries to understand how the brokerage window works (*e.g.*, how and to whom to give investment instructions; account balance requirements, if any; restrictions or limitations on trading, if any; how the brokerage window differs from the plan's designated investment alternatives) and who to contact with questions. See FAB 2012-02R at Q&A 13. Do these disclosures regarding how the brokerage window differs from the plan's designated investment alternatives typically include a description of the different risks and costs of investing through a brokerage window compared to investing in a designated investment alternative? Also, do the disclosures typically include a description of differences in fiduciary duties owed to participants investing through a brokerage window compared to investing in a designated investment alternative?
32. In a recent report entitled, 401(k) PLANS: Improvements Can Be Made to Better Protect Participants in Managed Accounts, GAO-14-310 (June 2014), the United States Government Accountability Office (GAO) recognized that managed account or similar services could be available to participants through brokerage windows. GAO recommended that the Department, among other things, amend regulations under title I of ERISA to require plan sponsors who offer managed account services to provide participants with standardized performance and benchmarking information on managed accounts. For example, one GAO suggestion is that plan officials could be required to

periodically furnish each managed account participant with the aggregate performance of participants' managed account portfolios and returns for broad-based securities market indices and applicable customized benchmarks. To what extent is the GAO recommendation feasible and advisable for participants who access managed account services with or without a brokerage window?

The Role of Advisers.

33. How often do plan fiduciaries engage advisers to assist with decisions about whether, and what type of brokerage window to include in their plan?
34. How often do plan participants use an adviser or a provider of managed account services to help them make investments through a plan brokerage window?
35. Do plans generally make advisers or managed account providers available to participants for this purpose and, if so, do the advisers or managed account providers typically contract with the plan or with the participant?
36. How often do plan participants independently select advisers or other providers to assist with their investments through the brokerage window? Are plan fiduciaries, recordkeepers, or other service providers generally aware of these arrangements?

Fiduciary Duties.

In connection with the issuance of FAB 2012-02 and FAB 2012-02R, the Department became aware of the possibility that plan fiduciaries and service providers have questions regarding the

nature and extent of ERISA's fiduciary of duties under section 404(a) of ERISA in connection with brokerage windows in plans intended to be "ERISA 404(c) plans."

37. Do these questions indicate a need for guidance, regulatory or otherwise, on brokerage windows under ERISA's fiduciary provisions? For instance, is there a need to clarify the extent of a fiduciary's duties of prudence, loyalty, and diversification under section 404(a) of ERISA, both with respect to brokerage window itself, as a plan feature, and with respect to the investments through the window? If guidance is needed, please try to identify the precise circumstances in need of guidance. If no guidance is needed, please explain why not.

Annual Reporting and Periodic Pension Benefit Statements.

38. The annual reporting requirements contain a special provision for plans with brokerage windows. Specifically, subject to certain exceptions, the Schedule H allows plans to report certain classes of investments made through a brokerage window as an aggregate amount under a catch-all "other" category rather than by type of asset on the appropriate line item from the asset category, *e.g.*, common stocks, mutual funds, employer securities, etc. Should this special provision be changed to require more detail and transparency regarding these investments? If so, what level of transparency is appropriate, taking into account current technology and the administrative burdens and costs of increased transparency?

39. ERISA section 105 requires plans to furnish benefit statements at least quarterly in the case of participant-directed individual account plans. How do these benefit statements typically reflect investments made through brokerage windows?

Signed at Washington, D.C., this 7th day of August, 2014.

Phyllis C. Borzi
Assistant Secretary
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Billing Code 4510-29-P

[FR Doc. 2014-19832 Filed 08/20/2014 at 8:45 am; Publication Date: 08/21/2014]